



California Public Employees' Retirement System
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Agenda Item 5

September 12, 2011

TO: MEMBERS OF THE INVESTMENT COMMITTEE

- I. **SUBJECT:** Contracts - Affiliate Investment Programs
Multi-Strategy Index Fund Request for Proposal
- II. **PROGRAM:** Affiliate Investment Programs Division
- III. **RECOMMENDATION:** Approve issuance of a Request for Proposal (RFP) for passive fund management services

IV. ANALYSIS:

The CalPERS Board administers various trust funds, including defined benefit, defined contribution, deferred compensation, long-term care, and prefunding of other post-employment benefits (OPEB) plans.

A recent IRS Revenue Ruling (2011-1) updated the rules governing group trusts by clarifying that assets of certain governmental retirement and retiree benefits plans may be pooled in a group trust. To facilitate utilizing a group trust for certain retirement and retiree benefit assets, staff will no longer co-invest assets that cannot be pooled in a group trust. Separating the assets that cannot be pooled will result in the need to manage 10 additional portfolios.

At this time, the Investment Office does not have the capacity to manage the additional portfolios internally and thus is requesting approval to issue a Request for Proposal (RFP) for an external manager for the following portfolios:

- Long-Term Care Fund – all portfolios
- Health Care Fund – the nominal bond portfolio
- California Employers' Retiree Benefit Trust Fund (CERBT) – equity and real estate investment trust (REIT) portfolios
- CalPERS 457 Plan – the nominal bond portfolio
- State Peace Officers' & Firefighters' (POFF) Plan – the nominal bond portfolio
- Supplemental Contributions Program – the nominal bond portfolio

Additional funds may be added to this list should external management offer a more cost efficient, less complex solution than the internally managed group trust alternative. The Investment Office will consider transitioning these assets back to internal management after implementation of its target operating model, which is focused on building a more scalable infrastructure with stronger controls.

To hire an external manager, staff requests to issue a RFP for external investment management services and will return to the Investment Committee for approval to hire the recommended finalist. The recommended firm will provide low cost passive index asset management services across multiple asset classes including global equity, fixed income, treasury inflation protected securities (TIPS), commodities and REIT portfolios. Key steps and anticipated dates are as follows:

1. Fall 2011 – release RFP
2. Late Fall 2011 – finalist(s) evaluation and interviews with staff
3. Winter 2011 – staff presents finalist(s) to the Investment Committee for approval
4. Spring 2012 – anticipated movement of assets to external manager

V. STRATEGIC PLAN:

These initiatives address two CalPERS Strategic Plan Goals:

- Goal VIII to manage the risk and volatility of assets and liabilities to ensure sufficient funds are available, first, to pay benefits and second, to minimize and stabilize contributions; and
- Goal IX to achieve long-term, sustainable, risk adjusted returns.

VI. RESULTS/COSTS:

Staff expects the external investment manager costs to be relatively low due to the use of passive investment strategies and the economies of scale from the total asset value of \$5.3 billion. Costs will be paid by the related trust funds.

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Members of the Investment Committee
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